

BEFORE THE  
POSTAL RATE COMMISSION  
WASHINGTON, D.C. 20268-0001

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POSTAL RATE COMMISSION  
OFFICE OF THE SECRETARY

POSTAL RATE AND FEE CHANGES, 1997

Docket No. R97-1

NOTICE OF UNITED STATES POSTAL SERVICE OF FILING OF ERRATA TO  
TESTIMONY OF WITNESS LION (USPS-T-24), TESTIMONY AND EXHIBITS OF  
WITNESS SECKAR (USPS-T-26), WORKPAPERS OF WITNESS TAUFIQUE (USPS-  
T-34), TESTIMONY AND WORKPAPERS OF WITNESS KANEER (USPS-T-35), AND  
CORRECTED DISKETTE FOR LIBRARY REFERENCE H-205  
(August 14, 1997)

The United States Postal Service hereby provides notice that it is today filing errata to the testimony of witness Lion (USPS-T-24), the testimony and exhibits of witness Seckar (USPS-T-26), the workpapers of witness Taufique (USPS-T-34), and the testimony and workpapers of witness Kaneer (USPS-T-35). A corrected diskette containing machine readable versions of witnesses Kaneer's and Taufique's workpapers is also being filed in Library Reference H-205. These revisions, which are described in the attached summaries, clarify the workpapers, correct some citations, and provide some minor editorial and substantive corrections. Witness Lion's errata slightly reduce costs presented in his Table 13. In addition, a hard copy of Kaneer Workpaper E page 2, which could be produced using the machine readable files underlying witness Kaneer's workpapers in Library Reference H-205, is also provided. Revised copies of witnesses Lion's, Seckar's and Kaneer's testimony and exhibits are attached to this Notice, and revised pages of witnesses Kaneer's and Taufique's workpapers (and the diskette) are filed with the Commission and provided to the Postal


Service library. With the exception of witness Lion, all substantive corrections are shaded.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

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\_\_\_\_\_  
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**ERRATA  
USPS T-24  
DOCKET NO. R97-1**

1. Page 8, line 11, reads:

*"Presiding Officer's Information Request No. 6, Question 4"*

should read

*"Presiding Officer's Information Request No. 4, Question 6".*

2. Page 11, line 10:

*"\$16.9 million" should read "\$21.9 million"*

*"\$595.7 million" should read "\$585.6 million"*

Page 11, lines 10-11, reads:

*"2.9 percent" should read "3.9 percent"*

Page 11, line 11, reads

*"16.0 million" should read "15.9 million"*

Page 11, lines 10-11, reads:

*"2.0 percent" should read "2.1 percent"*

3. Page 15, replace Table 7D with new Table 7D (attached). The line "Caller Service" has been corrected. Specifically:

*"Pre 96-3 Fees" reads "\$451" should read "\$349".*

*"Pct. Change" reads "0%" should read "29%"*

*"Pre 96-3 Boxes" reads "110,370" should read "100,770"*

*"Elasticity" reads "[blank]" should read "-0.398"*

*"Post 96-3 Boxes" reads "110,370" should read "89,055"*

*"Pre 96-3 Revenues" reads "\$49,776,870" should read "\$35,168,730"*

*"Post 96-3 Revenues" reads "\$49,776,870" should read "\$40,163,805"*

*"Change in Revenues" reads "\$0" should read "\$4,995,075"*

The row "Reserve Numbers" has also been corrected. Specifically:

"Pre 96-3 Boxes" reads "195,742" should read "178,717"

"Post 96-3 Boxes" reads "195,742" should read "178,717"

"Pre 96-3 Revenues" reads "\$5,872,260" should read "\$5,361,510"

"Post 96-3 Revenues" reads "\$5,872,260" should read "\$5,361,510"

The row "Grand Total" has also been changed to reflect these corrections.

4. Page 18, replace Table 9B with new Table 9B (attached). The line "Caller Service" has been corrected to reflect the changes in Table 7D. Specifically:

"TYBR Number of Boxes" reads "102,185" should read "90,747"

"Elasticity" reads "-0.517" should read "-0.431".

"TYAR Number of Boxes" reads "90,596" should read "82,161"

"TYBR Revenues" reads "\$46,085,579" should read \$40,926,917"

"TYAR Revenues" reads "\$49,827,932" should read "\$45,188,468"

Change in Revenues" reads "\$3,742,353" should read "\$4,261,551"

The row "Grand Total" has also been changed to reflect this correction.

5. Page 22, line 12, Equation (2)

$$c = (\$179,233,000) / Q$$

should read

$$c = (\$223,226,000) / Q$$

6. Page 22, lines 15-16: Strike the sentence:

"The constant "c" can be interpreted as the cost for a "basic" unit of capacity and, in this case, equals \$1.52."

The interpretation is incorrect. This does not change any other results or conclusions.

7. Page 26, replace Table 12 with new Table 12 (attached). The changes in this table are a result of the revised calculation of average rent as explained in the errata to USPS LR-H-188. The only columns that changed are the column labeled "Average Rent" and the two columns to its right, labeled "Total Costs (thousands)" and "Costs per Box".
8. Page 27, replace Table 13 with new Table 13 (attached). The changes in this table are a result of the revised calculation of average rent as explained in the errata to USPS LR-H-188. The only columns that changed are those labeled "Space Provision" and "Costs per Box".
9. A further correction to Tables 12 and 13 results from the fact that coefficient "c" in equation (1), page 22, was incorrectly calculated as 1.52. The correct value is 1.436. This correction affects the columns labeled "Total Costs (Thousands)" and "Costs per Box" in Table 12, and the columns labeled "Space Provision" and "Costs per Box" in Table 13. This does not affect any other conclusions or results.

**Table 4. Estimated Boxes in Use, Pre-MC96-3**

<b>Carrier Delivery Group</b>						
<b>Box Size</b>	<b>City - A</b>	<b>City - B</b>	<b>City - other</b>	<b>Non-city</b>	<b>Non-Delivery</b>	<b>Total</b>
1	70,784	121,923	5,244,919	3,681,614	951,038	10,070,279
2	4,416	29,279	2,220,343	1,532,607	326,535	4,113,180
3	2,477	10,543	736,247	400,829	78,499	1,228,595
4	258	1,649	157,159	32,027	6,397	197,490
5	75	1,659	32,895	3,560	729	38,918
<b>Total</b>	<b>78,010</b>	<b>165,053</b>	<b>8,391,563</b>	<b>5,650,638</b>	<b>1,363,197</b>	<b>15,648,462</b>

In order to estimate the effect of the fee changes established in MC96-3, it is next necessary to regroup the boxes in Table 4 into the new fee groups (as opposed to delivery groups), since this is now how fees are prescribed. Delivery Groups City-A and City-B, both defined in terms of specific ZIP Codes, translate directly into Fee Groups A and B, respectively. However, the three "lower" groups each have some customers who are ineligible for carrier delivery and who are thus entitled to a post office box at no fee. The numbers of these ineligible customers were estimated in the Postal Service's response to the Presiding Officer's Information Request No. 4, Question 6, in Docket No. MC96-3. The midpoints of those estimates have been used in these calculations.

Table 5 below presents the assumptions for Fee Groups C, D, and E. Several new subgroups are defined. These subgroups must be kept distinct

<b>Table 6C. Estimated Boxes in Use, Pre-MC96-3</b>			
<b>All Boxes</b>			
<b>Box Size</b>	<b>Paid Boxes</b>	<b>Free Boxes</b>	<b>Total</b>
<b>1</b>	<b>9,464,496</b>	<b>605,782</b>	<b>10,070,279</b>
<b>2</b>	<b>3,881,442</b>	<b>231,738</b>	<b>4,113,180</b>
<b>3</b>	<b>1,168,503</b>	<b>60,093</b>	<b>1,228,595</b>
<b>4</b>	<b>191,668</b>	<b>5,822</b>	<b>197,490</b>
<b>5</b>	<b>38,111</b>	<b>807</b>	<b>38,918</b>
<b>Total</b>	<b>14,744,220</b>	<b>904,241</b>	<b>15,648,462</b>

### C. ESTIMATION OF POST-MC96-3 BOXES

The final step is to apply price elasticities to estimate the effect of the new fees on each subgroup.<sup>2</sup> This information is presented in Tables 7A-D on the next four pages. Table 7A shows the results for Fee Groups A, B, and C. Tables 7B and 7C show the results for Fee Groups D and E respectively; Table 7D summarizes the results for all fee groups, plus caller service and reserve numbers. In addition to the Post-MC96-3 box counts, these tables estimate the resulting revenue change. Because of the fee increases, revenue for post office boxes is projected to increase by \$21.9 million to \$585.6 million annually (or 3.9 percent). The total box count decreases from 15.9 million to 15.6 million (or 2.1 percent).

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<sup>2</sup> The elasticities used are from Postal Rate Commission's *Opinion and Recommended Decision* in Docket No. MC96-3, Appendix D, Schedule 3, page 17.

**Table 7D. Estimated Boxes in Use by Fee Group, Post-MC96-3**

**All Fee Groups plus Caller Service and Reserve Numbers**

Fee Group	Box Size	Pre 96-3 Fees	Post 96-3 Fees	Pct. Change	Pre 96-3 Boxes	Elasticity	Post 96-3 Boxes	Pre 96-3 Revenues	Post 96-3 Revenues	Change in Revenues
<b>Paid Boxes (A+B+C+D)</b>					14,744,220		14,425,267	\$516,190,819	\$540,041,358	\$23,850,539
<b>Free Boxes (E)</b>					904,241		904,241	\$6,902,558	\$0	(\$6,902,558)
<b>Total Boxes</b>					15,648,462		15,329,509	\$523,093,377	\$540,041,358	\$16,947,981
<b>Caller Service</b>		\$349	\$451	29%	100,770	-0.398	89,055	\$35,168,730	\$40,163,805	\$4,995,075
<b>Reserve Numbers</b>		\$30	\$30	0%	178,717		178,717	\$5,361,510	\$5,361,510	\$0
<b>Grand Total</b>					15,927,949		15,597,281	\$563,623,617	\$585,566,673	\$21,943,056

**Table 9B. Estimated Boxes In Use by Fee Group, TYAR**

Summary plus Caller Service & Reserve Numbers

Fee Group	Box Size	Current Fee	New Fee	Pct. Change	TYBR Number of Boxes	Elasticity	TYAR Number of Boxes	TYBR Revenues	TYAR Revenues	Change in Revenues
Paid Boxes		\$38	\$45	34%	14,699,347	-0.155	13,918,498	\$564,970,441	\$632,144,039	\$67,173,598
Free Boxes (E)					921,422		921,422	\$0	\$0	\$0
Total Boxes		\$36	\$43	34%	15,620,769	-0.146	14,839,920	\$564,970,441	\$632,144,039	\$67,173,598
Caller Service		\$451	\$550	22%	90,747	-0.431	82,161	\$40,926,917	\$45,188,468	\$4,261,551
Reserve Numbers		\$30	\$40	33%	182,113	-0.517	150,749	\$5,463,379	\$6,029,976	\$566,598
Grand Total								\$611,360,737	\$683,362,484	\$72,001,747

As discussed above, Space Provision costs vary proportionately with both box size (capacity) and with location (average rent). In mathematical terms, this can be expressed as:

$$AC_{jk} = c (R_j) (EC_{jk}) \quad (1)$$

where  $AC_{jk}$  is the volume-variable cost for fee group  $j$  and box size  $k$ ,  $R_j$  is average cost per square foot for fee group  $j$ , and  $EC_{jk}$  is the equivalent capacity for fee group  $j$  and box size  $k$ . The constant of proportionality ( $c$ ) is determined so as to make the sum over all fee groups and box sizes equal the volume-variable cost for space provision (\$223.2 million). Since the average rents are the same for all box sizes in a given fee group, this constant can be calculated from the expression:

$$c = (\$223,226,000) / Q \quad (2)$$

where  $Q = R_A E_A + R_B E_B + \dots + R_E E_E$ . In this expression  $E_j$  refers to the total equivalent capacity for fee group  $j$  ( $E_j = \sum_k EC_{jk}$ ). The corresponding rents are in contained in Table 12.

The cost per box is calculated by dividing  $AC_{jk}$  by the number of boxes in that fee group and box size. Therefore, it can also be calculated directly from the expression:

$$ac_{jk} = c (R_j) (CF_k) \quad (3)$$

where  $ac_{jk}$  is the volume-variable cost per box for fee group  $j$  and box size  $k$ , and  $CF_k$  is the capacity factor for box size  $k$ . The resulting unit costs vary with both box size and fee group, as shown in Table 12.

Table 12. ALLOCATION OF SPACE PROVISION COSTS

Fee Group	Box Size	No. of Boxes	Cap. Factor	Equivalent Capacity	Percentage of Equivalent	Average Rent	Total Costs (thousands)	Costs Per Box
A	1	72,129	1	72,129	0.3351%	\$23.49	\$2,433	\$33.72
	2	4,500	1.5	6,750	0.0314%	\$23.49	\$228	\$50.59
	3	2,524	3	7,571	0.0352%	\$23.49	\$255	\$101.17
	4	242	6	1,453	0.0067%	\$23.49	\$49	\$202.35
	5	69	12	824	0.0038%	\$23.49	\$28	\$404.70
	Total	79,464	1.12	88,728	0.41%	\$23.49	\$2,992	\$37.66
B	1	124,239	1	124,239	0.5773%	\$16.74	\$2,986	\$24.03
	2	29,835	1.5	44,752	0.2079%	\$16.74	\$1,076	\$36.05
	3	10,744	3	32,231	0.1498%	\$16.74	\$775	\$72.10
	4	1,553	6	9,315	0.0433%	\$16.74	\$224	\$144.20
	5	1,516	12	18,189	0.0845%	\$16.74	\$437	\$288.41
	Total	167,886	1.36	228,728	1.06%	\$16.74	\$5,497	\$32.74
C	1	5,291,127	1	5,291,127	24.5846%	\$7.71	\$58,569	\$11.07
	2	2,239,904	1.5	3,359,857	15.6112%	\$7.71	\$37,191	\$16.60
	3	742,733	3	2,228,199	10.3531%	\$7.71	\$24,665	\$33.21
	4	158,544	6	951,264	4.4199%	\$7.71	\$10,530	\$66.42
	5	33,185	12	398,218	1.8503%	\$7.71	\$4,408	\$132.83
	Total	8,465,493	1.44	12,228,664	56.82%	\$7.71	\$135,363	\$15.99
D	1	3,985,837	1	3,985,837	18.5197%	\$6.00	\$34,335	\$8.61
	2	1,561,215	1.5	2,341,823	10.8810%	\$6.00	\$20,173	\$12.92
	3	403,555	3	1,210,666	5.6252%	\$6.00	\$10,429	\$25.84
	4	32,290	6	193,739	0.9002%	\$6.00	\$1,669	\$51.69
	5	3,607	12	43,283	0.2011%	\$6.00	\$373	\$103.37
	Total	5,986,504	1.30	7,775,348	36.13%	\$6.00	\$66,979	\$11.19
E	1	617,292	1	617,292	2.8682%	\$7.19	\$6,372	\$10.32
	2	236,141	1.5	354,211	1.6458%	\$7.19	\$3,656	\$15.48
	3	61,234	3	183,703	0.8536%	\$7.19	\$1,896	\$30.97
	4	5,933	6	35,597	0.1654%	\$7.19	\$367	\$61.94
	5	822	12	9,865	0.0458%	\$7.19	\$102	\$123.87
	Total	921,422	1.30	1,200,668	5.58%	\$7.19	\$12,394	\$13.45
GRAND TOTAL		15,620,769	1.38	21,522,135	100%		\$223,226	\$14.29

**Table 13. TOTAL VOLUME-VARIABLE COSTS PER BOX**

<b>Fee Group</b>	<b>Box Size</b>	<b>No. of Boxes</b>	<b>Space Provision</b>	<b>Space Support</b>	<b>All Other</b>	<b>Costs Per Box</b>
<b>A</b>	1	72,129	\$33.72	\$13.01	\$6.69	\$53.43
	2	4,500	\$50.59	\$19.51	\$6.69	\$76.79
	3	2,524	\$101.17	\$39.02	\$6.69	\$146.89
	4	242	\$202.35	\$78.04	\$6.69	\$287.08
	5	69	\$404.70	\$156.08	\$6.69	\$567.47
	<b>Total</b>	<b>79,464</b>	<b>\$37.66</b>	<b>\$14.52</b>	<b>\$6.69</b>	<b>\$58.87</b>
<b>B</b>	1	124,239	\$24.03	\$13.01	\$6.69	\$43.74
	2	29,835	\$36.05	\$19.51	\$6.69	\$62.26
	3	10,744	\$72.10	\$39.02	\$6.69	\$117.82
	4	1,553	\$144.20	\$78.04	\$6.69	\$228.94
	5	1,516	\$288.41	\$156.08	\$6.69	\$451.18
	<b>Total</b>	<b>167,886</b>	<b>\$32.74</b>	<b>\$17.72</b>	<b>\$6.69</b>	<b>\$57.16</b>
<b>C</b>	1	5,291,127	\$11.07	\$13.01	\$6.69	\$30.77
	2	2,239,904	\$16.60	\$19.51	\$6.69	\$42.81
	3	742,733	\$33.21	\$39.02	\$6.69	\$78.92
	4	158,544	\$66.42	\$78.04	\$6.69	\$151.15
	5	33,185	\$132.83	\$156.08	\$6.69	\$295.61
	<b>Total</b>	<b>8,465,493</b>	<b>\$15.99</b>	<b>\$18.79</b>	<b>\$6.69</b>	<b>\$41.47</b>
<b>D</b>	1	3,985,837	\$8.61	\$13.01	\$6.69	\$28.32
	2	1,561,215	\$12.92	\$19.51	\$6.69	\$39.13
	3	403,555	\$25.84	\$39.02	\$6.69	\$71.56
	4	32,290	\$51.69	\$78.04	\$6.69	\$136.42
	5	3,607	\$103.37	\$156.08	\$6.69	\$266.14
	<b>Total</b>	<b>5,986,504</b>	<b>\$11.19</b>	<b>\$16.89</b>	<b>\$6.69</b>	<b>\$34.78</b>
<b>E</b>	1	617,292	\$10.32	\$13.01	\$6.69	\$30.02
	2	236,141	\$15.48	\$19.51	\$6.69	\$41.69
	3	61,234	\$30.97	\$39.02	\$6.69	\$76.68
	4	5,933	\$61.94	\$78.04	\$6.69	\$146.67
	5	822	\$123.87	\$156.08	\$6.69	\$286.65
	<b>Total</b>	<b>921,422</b>	<b>\$13.45</b>	<b>\$16.95</b>	<b>\$6.69</b>	<b>\$37.09</b>
<b>GRAND TOTAL</b>		<b>15,620,769</b>	<b>\$14.29</b>	<b>\$17.92</b>	<b>\$6.69</b>	<b>\$38.91</b>

### **Errata To USPS-T-26, Docket No. R97-1**

Page 11: At line 7, ADC (Area Distribution Center) is added as an operation at which a flat could receive handling. This was mistakenly omitted in the original text.

Page 15: At line 18, footnote #6 is deleted as it was not needed.


Page 4 of Exhibit J: The Applicable Rates for nonautomated basic mail on pallets in the non-unique 3-digit, unique 3-digit, optional city, and 5-digit package presort levels were changed from B [basic] to 3 [3-digit], 3, 3, and 5 [5-digit] respectively.

Page 5 of Exhibit J: The Applicable Rates for nonautomated basic mail on pallets in the 3-digit and 5-digit package presort levels are changed from B [basic] to 3/5 [3/5 digit] in both cases.

The changes made to Exhibit J are corrections to previously mislabeled rates in the original testimony filing.

Piece distribution costs for each of the rate categories of flats listed in Section II are developed through the use of mail flow models that estimate the number of piece handlings a flat receives at each operation, as well as the cost. The operations are as follows.

- outgoing primary,
- outgoing secondary,

- 
- SCF,
  - incoming primary, and
  - incoming secondary

Bundle sorting unit costs for each of the rate categories of flats listed in Section II are developed through the use of a model which estimates the number of handlings or opening units that flats bundles receive or pass through, according to the presort makeup of the bundles.

All other volume variable mail processing costs are obtained through the manipulation of benchmark costs and a combination of piece distribution and bundle sorting costs.<sup>3</sup> Benchmark costs are shape and subclass specific, and contain all CRA test year volume variable mail processing costs. These costs are inputs to this testimony and are detailed in LR-H-106.

The rate category-specific piece distribution and bundle sorting costs are weighted together to form a weighted modeled cost of the flats subclass. Thus, the weighted modeled cost represents a subset of the costs contained in its corresponding benchmark. The weighted modeled cost is applied to the worksharing related portion of the benchmark costs to develop an adjustment factor. The rate

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<sup>3</sup> The combination of the piece distribution and bundle sorting costs is referred to as the modeled cost.

1 category, allowing the differences between the categories to focus primarily on the  
2 effect of the mailer-applied barcode.

3  
4 B. DEVELOPMENT OF PIECE DISTRIBUTION COSTS

5  
6 This section of testimony discusses the general construct and methodology used  
7 to develop piece distribution costs. Piece distribution costs are those incurred in the  
8 mail processing operation by sorting mail pieces into piece distribution separations,  
9 such as in manual casing of flats or FSM-881 sorts.

10  
11 1) MODEL CONSTRUCT

12  
13 Piece distribution costs are developed for each of the non-carrier route rate  
14 categories listed in Section II. The *nonautomation rate categories* are disaggregated  
15 into machinable and nonmachinable categories for modeling purposes.

16 Presort categories correspond to the presort level to which mail is sorted by  
17 mailers before deposit into the mail stream. Acceptable levels of presort for flats mail  
18 are basic, 3-digit, and 5-digit; or 3/5-digit. Separate 3-digit and 5-digit presort levels are  
19 being proposed for Periodicals Regular and Nonprofit mail as part of this docket. The  
20 combined 3/5-digit presort level remains for First-Class Mail and Standard Mail (A) flats.  
21 A summary of allowable presort compositions is provided in Exhibit USPS-T-26J.

**TABLE A-2**  
**SUMMARY OF ALLOWABLE MAIL PRESORT COMPOSITION OF**  
**PERIODICALS REGULAR AND NONPROFIT FLATS MAIL**

			Applicable Rates	
	Container Presort Level	Package Presort Level	In Sack	On Pallet
Automation	Basic	Mixed ADC	B	B
		ADC	B	B
		non-unique 3-digit	3	3
		unique 3-digit	3	3
		optional city	3	3
		5-digit	5	5
	3-Digit	non-unique 3-digit	3	3
		unique 3-digit	3	3
		optional city	3	3
		5-digit	5	5
	5-Digit	5-digit	5	5
	Nonautomation	Basic	Mixed ADC	B
ADC			B	B
non-unique 3-digit			B	
unique 3-digit			B	
optional city			B	
5-digit			B	
3-Digit		non-unique 3-digit	3	3
		unique 3-digit	3	3
		optional city	3	3
		5-digit	5	5
5-Digit		5-digit	5	5
B = basic rate, 3 = 3-digit presort rate, 5 = 5-digit presort rate, CR = carrier route presort rate				

**TABLE A-3**  
**SUMMARY OF ALLOWABLE MAIL PRESORT COMPOSITION OF**  
**STANDARD (A) REGULAR AND NONPROFIT FLATS MAIL**

			Applicable Rates	
	Container Presort Level	Package Presort Level	In Sack	On Pallet
Automation	Basic	Mixed ADC	B	B
		ADC	B	B
	3/5-Digit	3-digit	3/5	3/5
		5-digit	3/5	3/5
		3-digit	3/5	3/5
		5-digit	3/5	3/5
Nonautomation	Basic	Mixed ADC	B	B
		ADC	B	B
		3-digit	B	
		5-digit	B	
	3/5-Digit	3-digit	3/5	3/5
		5-digit	3/5	3/5
B = basic rate, 3/5 = 3/5-digit presort rate				

**USPS-T-34 - Workpapers**  
**Witness Altaf Taufique**  
**ERRATA**

**Note: All changes described below are highlighted on the workpapers.**

**I. WP RR-C, p 1, Changes:**

Advertizing Total to Advertising Total.

**Row Total Pounds, Column 100% Advertising**, \$1,634,392,219 deleted (not needed).

**Row Total Revenues Pieces & Pounds, Column 100% Advertising**, \$2,872,711,064 to \$2,055,514,954.

**Row Revenue \* PRW Adjustment Factor, Column 100% Advertising**, \$2,875,114,435 to \$2,057,234,642.

**Row Revenue with Fees, Column 100% Advertising**, \$2,889,765,435 to \$2,071,885,642.

**Row Cost Coverage, Column 100% Advertising**, 1.821731944 to 1.306133783.

**II. WP RR-D, p 1, Changes**

**Line 1, Column Source/Notes**, Base Year Volume: Billing Determinants Library Reference LR-H-145 to Billing Determinants Library Reference H-145.

**Line 2, Column Source/Notes**, TY Before Rates Volume: Library Reference LR-H-171 to USPS-T-6 p. 106.

**Line 3, Column Item**, TY Before Rates To Base Year Scalling Factor to TY Before Rates To Base Year Scaling Factor.

**Line 4, Column Source/Notes**, TY After Rates Volume: Library Reference LR-H-172 to USPS-T-6 p. 106.

**Line 12, Column Source/Notes**, TYBR Fees: changes from USPS-T-39 and USPS-T-40, Workpapers to USPS-T-30.

**Line 13, Column Amount**, TYAR Fees: \$14,693,000 to 14,598,000, **Column Source/Notes** USPS-T-39 and USPS-T-40, Workpapers to USPS-T-30.

**Line 15, Column Source/Notes**, Multiplier to Get Actual Revenue: changes from Billing Determinants Library Reference LR-H-145 to Billing Determinants Library Reference H-145

**Line 18**, Proportion of Transportation Cost that is Distance Related: changes from 0.786379058 to 0.7864 and Workpapers USPS-T-5, WP-B, Worksheet 14.0.7 changes to Workpapers USPS-T-5, WP-B, Worksheet 14 07b, p.2.

**III. WP RR-H, p 1, Changes**

Flat Mail Processing Cost Estimates Chart: USPS-T-23 to Ex. USPS-26F, p 2 of 7.

**IV. WP RR-J, p 1, Changes**

**Fee Revenue**: from \$14,693,000 to \$14,598,000.

**Total Revenue including Fees**: from \$1,689,040,053 to \$1,688,945,053, **Cost Coverage**: from 1.06969 to 1 06963.

**V. WP RR-N, p 1, Changes Volumes From Mail Characteristic Study:**

Add footnote 1 after Volumes From Mail Characteristic Study, to read  
Source: WP RR-M

**VI WP-RR-N, p 3, Changes Allocation of Non-Automated Pieces:**

Basic Non-Automation 0.1 to 14.2%, 3-Digit Non-Automation 0.4 to 39 6%, 5-Digit Non-Automation 0.5 to 46.2%

Allocation of Automation Pieces: changes from Basic Automation 0.1 to 6.1%, 3-Digit Automation 0.3 to 32.7%, 5-Digit Automation 0.6 to 61.2%  
Also Omitted: Column numbers. Notes at the bottom of the chart: Col. (2) = distribution of column (1), Col. (4) = Totals from Col. (3) distributed by Col. (2), and Source:  
Continuation From WP RR-N, pp 1-2.

- VII. **WP WC-C, p 1, Changes PERIODICALS** Within County Rate Design Inputs:  
    **Line 2**, TY Before Rates Volume LR-H-171 to USPS-T-6, p 106  
    **Line 4**, TY after Rates Volume LR-H-172 to USPS-T-6, p 106  
    **Line 16**, TYBR Fees Used In Rate Design USPS T-39 and USPS T-40, Workpapers to USPS T-30  
    **Line 17**, TYAR Fees \$1,719,000; USPS T-39 and USPS T-40 Workpapers to \$1,842,000; USPS T-30.
- VIII. **WP WC-I, p 1, Changes** Within County Rate Comparison Of Current And Proposed Rates:  
    Billing Determents Column deleted.
- IX. **WP WC-J, p1:** Insert omitted page.

**USPS-T-35**  
**Witness Kirk T. Kaneer**  
**SUMMARY OF REVISIONS**

- I. WP D, p1, line 17 - TYAR FEES:  
change \$4,442,000 to \$4,414,000.
- II. WP D, p2, line 7 - TYBR COST, WITHOUT CONTINGENCY:  
change 13,749,000 to 13,669,000,  
line 10 - TYBR COST, (Including Contingency)  
change 13,886,490 to 13,805,690
- III. WP D, p3, line 17 - TYAR FEES:  
change \$4,442,000 to \$4,414,000.
- IV. WP D, p4, line 7 - TYBR COST, WITHOUT CONTINGENCY:  
change 13,749,000 to 13,669,000,  
line 10 - TYBR COST, (Including Contingency):  
change 13,886,490 to 13,805,690.
- V. WP E, p2:  
page omitted - insert additional page 2.
- VI. WP J, p1, line 5 - Fee Revenue:  
change \$4,442,000 to \$4,414,000,  
line 6 - Revenue including fees:  
change 342,659,466 to 342,631,466,  
line 8 Cost Coverage:  
change 1.0330 to 1.029
- VII. WP K, p1, line 5 - Fee Revenue:  
change \$4,442,000 to \$4,414,000,  
line 6 - Revenue including fees:  
change 345,274,686 to 345,246,686.
- VIII. WP O, p1, line 7 - TYBR Cost:  
change 13,886,490 to 13,805,690,  
line 8 - Cost Coverage:  
change 819 to 824.
- IX. WP O, p2, line 7 - TYBR Cost:  
change 13,886,490 to 13,805,690,

line 8 - Cost Coverage.

change .824 to .829.

X. Testimony p1 - Table 1

Classroom Proposed Avg \$/Piece

change \$0.217 to \$0.222,

Classroom TYBR Cost Coverage

change 76.2% to 76.6%,

Classroom Proposed Cost Coverage

change 80.6 to 82.6,

Classroom Percentage Avg \$/Piece Increase,

change 4.8% to 7.2%.

XI. Testimony p6, line 14: change 7.8 to 7.7.

XII. Testimony p10, line 19 change 21.7 to 22.2,

XIII. Testimony p11,

line 8: change 21.7 to 22.2,

line 10: change 21.1 to 21.6,

line 17: change 21.1 to 21.6,

line 18: change 21.7 to 22.2.

XIV. Testimony p12,

line 12: change 21.1 to 21.6.

XV. Testimony p13,

line 13: change 5 percent to 7 percent.

XVI. Testimony p16,

Table 4 - Fee Revenue: change 4,442,000 to 4,414,000,

- Revenue including fees: change 342,659,466 to 342,631,466,

Table 5 - Total Revenue: change 10,150,746 to 10,403,626,

- RPW Adjusted Revenue 10,188,978 to 10,442,810,

- Cost Coverage: change 80.6% to 82.6%.

XVII. Workpaper Label and Citation Changes:

- WP-B, p6: increased "Col. 2" width to display 100% total value,
- WP-C, pp2-4: Changed source notation header (From Docket No. MC96-2, USPS LR-PRR-2 Diskette) to (From Second-Class Classroom Mail Characteristics Study Diskette),

- WP-D, p1-4, lines 2 & 4: changed Library Reference LR-H-171 to "USPS-T-6 p 106",  
line 13: changed "Source/Notes" column, from Step 5 (6) to STEP Factor,
- WP-D, p2: line 3, changed "Scalling" to "Scaling",
- WP-D, p3: line 13, Source/Notes col., from Step 6 to STEP Factor,
- WP-D, p4: line 3 changed "Scalling" to "Scaling",
- WP-H, p1: changed source for "Flat Mail Processing Cost Estimates" from " USPS-T-26" to  
"Source. Exhibit USPS-T-26G, p2.",
- WP-L, p1-2: changed testimony reference from "USPS-T-34" to "USPS-T-35."

## I. PURPOSE

This testimony presents the Postal Service's proposed rate design and changes in rate structure for Nonprofit Periodicals and Classroom subclasses. It begins with the highlights of the proposed average piece rates and cost coverages. Next, short descriptions of the user characteristics and volume trends are given, followed by explanations of the proposed classification changes and rate design. Lastly, this testimony justifies the application of Nonprofit rates to Classroom mail.

## II. TEST YEAR HIGHLIGHTS

In this proceeding, the Postal Service proposes a modest increase in Nonprofit and Classroom rates. The average price changes and cost coverages for the subclasses are as follows:<sup>1</sup>

Table 1: Test Year Rates and Cost Coverage Comparison.					
	TYBR Avg.\$/Piece	Proposed Avg.\$/Piece	TYBR Cost Coverage	Proposed Cost Coverage	Percentage Avg.\$/Piece Increase
<i>Nonprofit</i>	\$0.153	\$0.159	99.7%	103.3%	3.9%
<i>Classroom</i>	\$0.207	\$0.222	76.6%	82.6%	7.2%

<sup>1</sup> Rates are calculated inclusive of fees and reflect phase 5 rates applicable in the TY

**B. Nonprofit**

The Nonprofit rate design methodology for both pound and piece elements follows the methodology used to develop the corresponding rates in the Regular subclass. In setting Nonprofit discounts, most of the passthroughs are set at or near 100 percent; however, a few passthroughs were adjusted to moderate the impact of the rate changes on mailers. For example, the passthrough for 5-digit nonautomation was set at 83 percent of the 5-digit nonautomation cost savings to moderate the downward swing in the 5-digit rate, as well as mitigate the impact on the Basic rate. My workpapers provide detailed information on rate development for Nonprofit Periodicals, including revenue and cost coverage.

The proposed rates for Periodicals also incorporate a new and improved methodology for developing the nonadvertising, or "editorial," pound rate. Previously, the editorial pound rate was tied to the zone 1&2 advertising pound rates. The new methodology simply takes the revenue goal for Nonprofit that is to be derived from pound rates, excluding any markup, and divides this figure by the total number of Nonprofit pounds. The new methodology for developing the editorial pound rate is intended to yield a rate that, in combination with the revenue from the advertising pound rate, recovers the assigned revenue goal to be received from pound rates in Nonprofit. In this proceeding, however, the proposed editorial pound rate is made subject to a passthrough of 88.5 percent, in order to mitigate the impact of the rate increase on mailers. With this passthrough, the editorial pound rate would rise from 14.2 cents to 15.3 cents (Step 5), which represents an increase of 7.7 percent.

1 become 19.87 cents, 21.49 cents, and 19.88 cents. In terms of cost level, each of these  
2 is thus comparable to the 23.50-cent figure reported in the FY96 CRA Report.

3 One alternative is to take an average using all four available data points. The  
4 average of FY93, FY94, FY95, and FY96 figures, when each has been inflated to FY96  
5 cost levels, is 21.19 cents. Compared with the reported FY96 unit cost for Classroom of  
6 23.50 cents, this number is 2.31 cents, or approximately 10 percent, lower. Another  
7 alternative might be to simply reject the FY96 number as an outlier, and calculate the  
8 average using only the previous three years worth of data. This would produce an  
9 average unit cost of 20.41 cents. This is 3.09 cents, or approximately 13 percent, lower  
10 than 23.50 cents reported in the FY 96 CRA Report. Either of these figures (21.19  
11 cents, or 20.41 cents) may represent a better estimate of the FY96 unit costs for  
12 Classroom Mail rate-making purposes than the 23.50-cent figure reported in the CRA.

13 As noted above, because of costing methodological changes, figures for BY96  
14 and subsequent times are not directly comparable to figures for earlier periods,  
15 including FY96. There is, however, no reason to believe that whatever random  
16 variations might have caused the FY96 estimate for Classroom unit cost to be inflated  
17 would have had any different effect on the estimates for BY96, and subsequent  
18 estimates based on BY96. Therefore, it would appear quite reasonable to assume that,  
19 in percentage terms, the overestimate should be the same. This suggests that to infer  
20 the effects of applying either moving average approach, one would multiply the estimate  
21 in question (e.g., Classroom unit costs for BY 96 or TYAR) by the ratio of either  
22  $21.19/23.50$ , or  $20.41/23.50$ , depending on which averaging approach is favored. Thus,  
23 when the Nonprofit Periodicals rate schedule is applied to Classroom, the TYAR unit  
24 revenue is 22.2 cents. Using the rollforward based on BY 96 costs, the TYAR unit cost

is 26.9 cents. Revenues do not cover costs. But if the TYAR estimate is reduced by applying the three-observation ratio, the revised TYAR unit cost estimate is 23.4 cents. If the four-observation ratio is applied, the revised TYAR unit cost estimate is 24.3 cents. Although both of these figures are still above the TYAR unit revenue figure, they are substantially closer to that number than is the un-revised TYAR unit cost figure.

#### 4. Proposal

Under the circumstances presented in this proceeding, the Postal Service submits that it is appropriate to apply the Nonprofit Periodicals rates to Classroom mailings. As indicated above, if that rate schedule is applied, Classroom TYAR unit revenue is estimated at 22.2 cents. If that revenue were to generate the step 5 cost coverage for Classroom and Nonprofit Periodicals, 103 percent, true unit Classroom costs would have to be approximately 21.6 cents. Note that this is well in excess of the Nonprofit TYAR unit costs of approximately 15.3 cents. In other words, on a unit basis, Classroom mail can still be considerably more costly to handle than Nonprofit without invalidating the assumption that the Nonprofit rate schedule is also appropriate for Classroom. This is because the rate schedule is designed to yield higher revenues from higher cost pieces, and the higher cost Classroom pieces generate substantially more revenue, on a unit basis, than the lower cost Nonprofit pieces.

If we define the 21.6 cent unit cost figure (derived above as that necessary to meet the target cost coverage with unit revenues of 22.2 cents) as the "target" TYAR unit cost, it appears that such a figure is outside the range of TYAR unit cost figures based on the available CRA data, using either the most recent historical year, FY 1996, or any average of recent historical years. It may not, however, be outside of some

1 reasonable approximation of a confidence interval around the CRA estimate, given the  
2 very high Coefficient of Variation that indicates a degree of uncertainty associated with  
3 the direct mail processing cost estimate for Classroom. See Docket No. MC96-2,  
4 USPS-CT-2 at 6-7. Before abandoning any further efforts to reconcile the target TYAR  
5 unit cost with the available cost information, therefore, one additional avenue of  
6 research merits exploration. Rather than rely on inferences drawn from national  
7 sampling data, it may be possible to develop a model for Classroom costs, similar to the  
8 model developed for Nonprofit periodicals.

9 A model for Classroom costs could perhaps be most instructive when compared  
10 with the model for Nonprofit costs. For example, all indications are that Classroom mail  
11 unit costs are higher than Nonprofit unit costs. The critical question is, how much  
12 higher? Given Nonprofit unit costs of 15.3 cents, a cost difference of between 5 and 6  
13 cents would still leave us very much in the range of our target Classroom unit costs of  
14 21.6 cents. If successfully constructed, a model could inform us whether the  
15 characteristics of Classroom mail, compared with the characteristics of Nonprofit mail,  
16 would lead us to expect a cost difference of that magnitude, or of the greater magnitude  
17 reflected in the recently reported CRA costs.

18 Unfortunately, no model of Classroom mail costs is currently available.  
19 Moreover, constructing such a model would require having available useable  
20 information on the mail characteristics of Classroom, at levels of detail well above what  
21 is collected by existing postal data systems. The need for such information was not  
22 anticipated at a stage in the preparation for this case sufficiently early to allow the  
23 information to be obtained. Therefore, in developing the rate proposals, the Postal  
24 Service has no basis to know whether a cost model would support acceptance of the

1 hypothesis that the unit costs of Classroom are greater than those of Nonprofit only to  
2 the extent that the mail characteristics (and billing determinants) are different, or  
3 whether such a model would support rejection of such an hypothesis, as apparently  
4 suggested by recently reported CRA data.

5 In this case, the Postal Service proposes applying the rate schedule designed for  
6 Nonprofit Periodicals to Classroom mailings while awaiting further information from  
7 future modeling efforts. In essence, the Postal Service proposal would maintain  
8 separate subclass identity for Nonprofit and Classroom mail, but would apply the  
9 Nonprofit rates to Classroom mail for ratemaking purposes. This proposal is primarily  
10 guided by recent events involving Classroom and the effect on mailers. If Classroom  
11 mailers had experienced no rate increases since Docket No. R94-1 (except for step  
12 increases), the Postal Service would be more receptive to design separate rates for the  
13 Classroom subclass. Such rates, presumably, would reflect some variation of the CRA  
14 reported costs. The Postal Service, however, is most cognizant of the rate increases for  
15 Classroom mailers that will be implemented starting in FY98 as a result of Docket No.  
16 MC96-2. As shown by my testimony in Docket MC96-2, USPS-CT-3 at 10, the currently  
17 scheduled increases for Step 5 rates are substantial, with piece rates increasing in the  
18 25-30 percent range. The Classroom rates proposed in this case would impose an  
19 additional increase of approximately 7 percent at TY (Step 5) levels. At the conclusion  
20 of the TY, one additional increase will be imposed as the last step of phasing is  
21 implemented. The need to avoid any further substantial increases for this subclass at  
22 this time is obvious. Given these circumstances, I believe it most appropriate to  
23 examine whatever information that cost models can provide before attempting to  
24 determine whether additional increases of the size suggested by the 1996

**VIII. FINANCIAL ANALYSIS**

Tables 4 and 5 display the revenue, costs, and cost coverages for Nonprofit and Classroom at proposed Step 5 rates.

**TABLE 4: NONPROFIT FINANCIAL SUMMARY**

Total Revenue		\$338,099,190
Total Pieces	2,161,076,559	
RPW Adjustment Factor		100.035%
RPW Adjusted Revenue		\$338,217,466
Fee Revenue		\$6,414,000
Revenue including fees		\$344,631,466
TYAR Cost		\$331,724,400
Cost Coverage		103.3%

**TABLE 5: CLASSROOM FINANCIAL SUMMARY**

Total Revenue		\$10,403,626
Total Pieces	47,452,000	
RPW Adjustment Factor		100.377%
RPW Adjusted Revenue		\$10,442,810
Fee Revenue		\$97,000
Revenue including fees		\$10,539,810
TYAR Cost		\$12,763,370
Cost Coverage		82.6%

## CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.

A handwritten signature in cursive script that reads "David H. Rubin". The signature is written in dark ink and is positioned above a horizontal line.

David H. Rubin

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